

Commonwealth of Kentucky

Personnel Cabinet

July 8, 2005

Self-Insurance
Premium Contributions
Collective Bargaining
Retiree Medical
HRA/HSA Comparison



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Self-Insurance In State Benefits Programs

- More than 60% of the indemnity, POS, and PPO health plans offered by all 50 states are self-funded.

Percentage of Self-Funded Plans by Plan Type *	
Plan Type	Percentage
Indemnity	71%
POS	69%
PPO	64%
HMO	32%
*This includes plans with or without stop-loss insurance Source: 2003 Segal State Health Benefits Survey: Medical benefits for Employees and Retirees.	

Note: 1 Segal surveyed all 50 states. 39 states provided their enrollment packages and 34 states completed all or portions of the survey questionnaire

State/Employee Cost Splits – Average By State (2004 and 2005)

- State Employee Health Benefits – Average Monthly Medical Costs for the State versus the Employee (Page 1 of 3)

	2004		2005		Change 2004 to 2005	
Average State cost	\$	674.31 (46 states)	\$	739.43	9.7%	
Average Employee Contribution	\$	168.48 (41 states)	\$	180.12 (49 states)	6.9% (49 states)	
	State	Employee	State	Employee	State	Employee
AL	\$ 550.00	\$ 164.00	\$ 650.00	\$ 164.00	18.2%	0.0%
AK	\$ 705.00	\$ 162.00	\$ 763.00	\$ 195.00	8.2%	20.4%
AZ	\$ 620.78	\$ 125.00	\$ 718.00	\$ 125.00	15.7%	0.0%
AR	\$ 493.13	\$ 294.14	\$ 524.43	\$ 381.40	6.3%	29.7%
CA	\$ 756.00	\$ 38.00	\$ 728.00	\$ 144.64	-3.7%	280.6%
CO	\$ 310.62	varies	\$ 460.27	\$ 390.32	48.2%	N/A
CT	\$ 828.87	\$ 146.61	\$ 962.14	\$ 170.02	16.1%	16.0%
DE	\$ 825.52	varies	\$ 946.50	varies	14.7%	N/A
FL	\$ 590.30	\$ 175.14	\$ 666.84	\$ 175.14	13.0%	0.0%
GA	\$ 646.58	\$ 180.28	\$ 573.24	\$ 198.32	-11.3%	10.0%
HI	varies	varies	\$ 453.14	\$ 255.12	N/A	N/A
ID	\$ 457.58	\$ 81.00	\$ 525.02	\$ 80.00	14.7%	-1.2%
IL	\$ 887.28	\$ 223.50	\$ 1,061.51	\$ 223.50	19.6%	0.0%
IN	\$ 834.17	\$ 131.15	\$ 834.17	\$ 217.34	0.0%	65.7%
IA	\$ 777.90	\$ 229.98	\$ 881.06	\$ 222.56	13.3%	-3.2%
KS	\$ 513.58	\$ 402.36	\$ 541.45	\$ 435.86	5.4%	8.3%
KY	\$ 286.16	varies	\$ 394.80	\$ 251.36	38.0%	N/A
LA	\$ 492.86	\$ 298.82	\$ 570.64	\$ 347.08	15.8%	16.2%

Source: NCLS Website (May 2005)

The relative cost comparisons among states can be impacted by employees' elections of employee only versus family coverage tiers. The cost to Kentucky appears relatively lower than other states because 69 percent of Kentucky state employees elected employee only coverage tiers.

State/Employee Cost Splits – Average By State (2004 and 2005) (Cont.)

- State Employee Health Benefits – Average Monthly Medical Costs for the State versus the Employee (Page 2 of 3)

	2004		2005		Change 2004 to 2005	
Average State cost	\$	444.39 (46 states)	\$	494.35	11.2%	
Average Employee Contribution	\$	102.18 (41 states)	\$	98.96 (49 states)	-3.2% (49 states)	
	State	Employee	State	Employee	State	Employee
ME	varies	varies	\$ 1,080.16	\$ 326.10	N/A	N/A
MD	\$ 591.93	\$ 121.17	\$ 617.17	\$ 121.83	4.3%	0.5%
MA	\$ 1,083.74	\$ 270.94	\$ 937.58	\$ 234.39	-13.5%	-13.5%
MI	\$ 903.13	\$ 47.53	\$ 957.49	\$ 50.40	6.0%	6.0%
MN	\$ 848.39	\$ 93.21	\$ 976.84	\$ 107.32	15.1%	15.1%
MS	\$ 228.00	\$ 356.00	\$ 280.00	\$ 438.00	22.8%	23.0%
MO	\$ 829.00	\$ 272.00	\$ 898.00	\$ 237.00	8.3%	-12.9%
MT	\$ 410.00	varies	\$ 425.00	\$ 187.00	3.7%	N/A
NE	\$ 856.98	\$ 227.80	\$ 936.02	\$ 248.80	9.2%	9.2%
NV	\$ 495.68	\$ 270.95	\$ 862.81	\$ 138.05	74.1%	-49.0%
NH	\$ 1,304.40	\$ 0.00	\$ 1,682.62	\$ 0.00	29.0%	0.0%
NJ	\$ 742.27	\$ 0.00	\$ 764.58	\$ 0.00	3.0%	0.0%
NM	varies	varies	\$ 534.86	\$ 229.23	N/A	N/A
NY	\$ 707.60	\$ 158.57	\$ 759.16	\$ 169.98	7.3%	7.2%
NC	\$ 285.92	\$ 427.48	\$ 285.92	\$ 427.48	0.0%	0.0%

The relative cost comparisons among states can be impacted by employees' elections of employee only versus family coverage tiers. The cost to Kentucky appears relatively lower than other states because 69 percent of Kentucky state employees elected employee only coverage tiers.

State/Employee Cost Splits – Average By State (2004 and 2005) (Cont.)

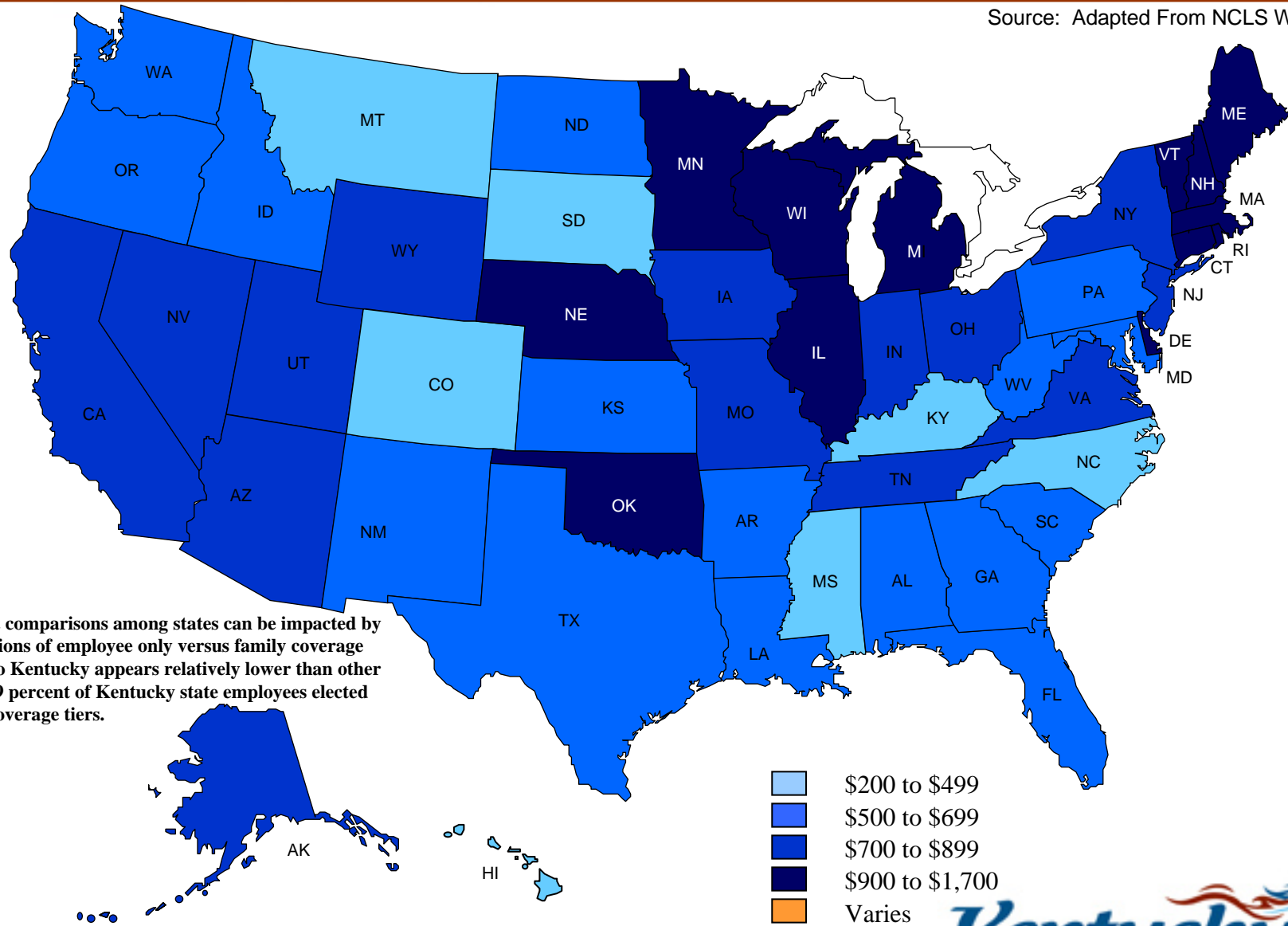
- State Employee Health Benefits – Average Monthly Medical Costs for the State versus the Employee (Page 3 of 3)

	2004		2005		Change 2004 to 2005	
Average State cost	\$	242.50 (46 states)	\$	254.39	4.9%	
Average Employee Contribution	\$	46.04 (41 states)	\$	39.46 (49 states)	-14.3% (49 states)	
	State	Employee	State	Employee	State	Employee
ND	\$ 488.70	\$ 0.00	\$ 567.52	\$ 0.00	16.1%	0.0%
OH	\$ 807.92	\$ 81.37	\$ 767.68	\$ 85.94	-5.0%	5.6%
OK	varies	varies	\$ 952.71	\$ 0.00	N/A	N/A
OR	\$ 721.62	\$ 0.00	\$ 531.97	\$ 0.00	-26.3%	0.0%
PA	\$ 509.17	\$ 22.44	\$ 585.00	\$ 147.41	14.9%	556.9%
RI	\$ 904.56	\$ 0.00	\$ 997.47	\$ 0.00	10.3%	0.0%
SC	\$ 466.72	\$ 234.68	\$ 503.46	\$ 294.58	7.9%	25.5%
SD	\$ 399.33	\$ 280.62	\$ 407.32	\$ 0.00	2.0%	-100.0%
TN	\$ 788.82	\$ 197.20	\$ 859.81	\$ 214.95	9.0%	9.0%
TX	\$ 586.39	\$ 286.12	\$ 616.36	\$ 300.79	5.1%	5.1%
UT	\$ 748.45	\$ 56.33	\$ 789.53	\$ 59.43	5.5%	5.5%
VT	\$ 1,055.62	\$ 263.91	\$ 1,140.09	\$ 285.02	8.0%	8.0%
VA	\$ 690.00	\$ 99.00	\$ 790.00	\$ 113.00	14.5%	14.1%
WA	\$ 518.00	\$ 90.00	\$ 637.00	\$ 101.00	23.0%	12.2%
WV	\$ 620.00	varies	\$ 632.00	\$ 87.00	1.9%	N/A
WI	\$ 1,021.21	\$ 89.67	\$ 1,113.11	\$ 125.00	9.0%	39.4%
WY	\$ 828.29	\$ 140.39	\$ 828.29	\$ 119.57	0.0%	-14.8%

The relative cost comparisons among states can be impacted by employees' elections of employee only versus family coverage tiers. The cost to Kentucky appears relatively lower than other states because 69 percent of Kentucky state employees elected employee only coverage tiers.

State/Employee Cost Split -- Average State Subsidy (2005)

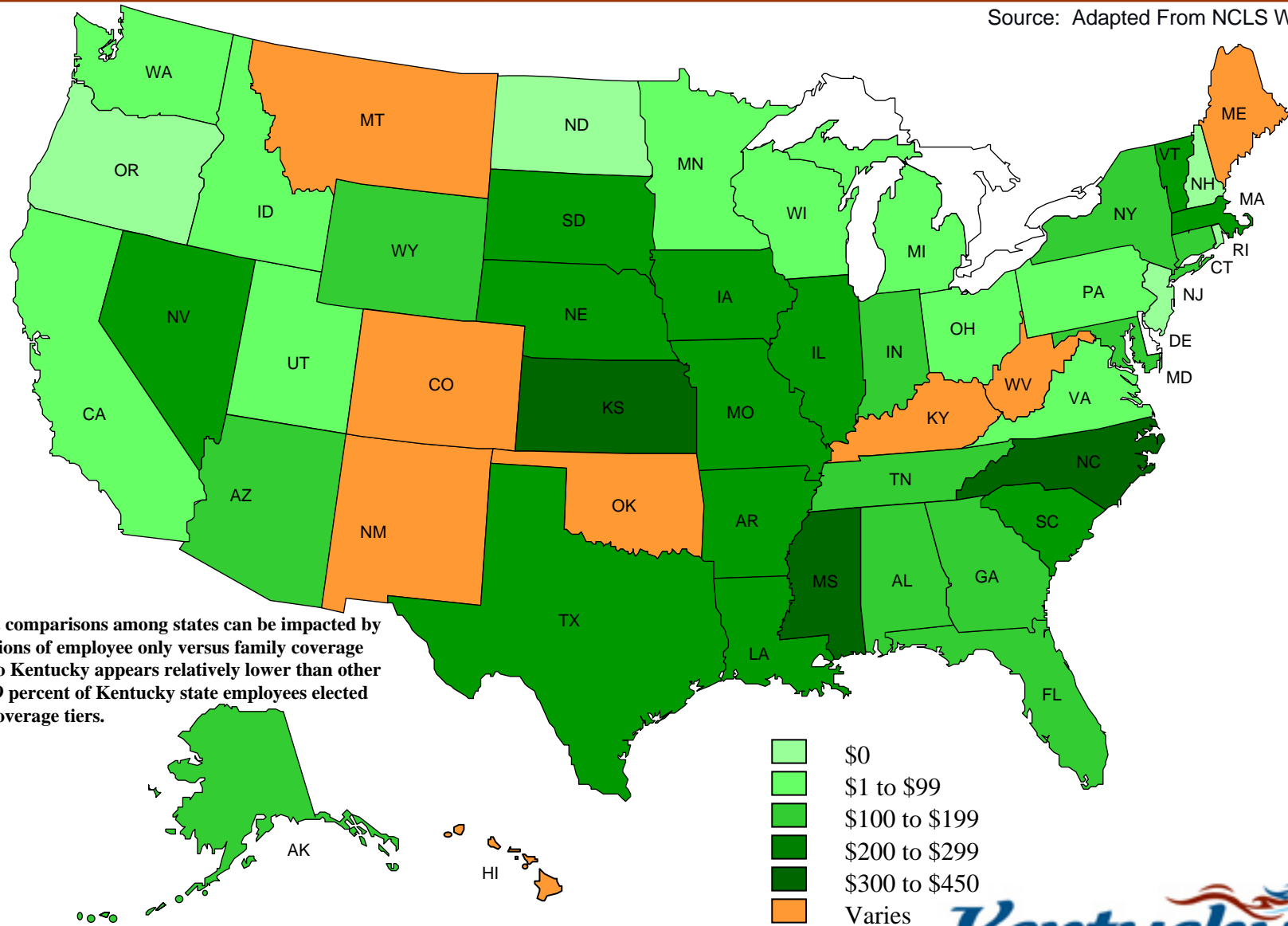
Source: Adapted From NCLS Website



The relative cost comparisons among states can be impacted by employees' elections of employee only versus family coverage tiers. The cost to Kentucky appears relatively lower than other states because 69 percent of Kentucky state employees elected employee only coverage tiers.

State/Employee Cost Splits – Average Employee Contribution (2005)

Source: Adapted From NCLS Website



The relative cost comparisons among states can be impacted by employees' elections of employee only versus family coverage tiers. The cost to Kentucky appears relatively lower than other states because 69 percent of Kentucky state employees elected employee only coverage tiers.

Collective Bargaining

Fewer than half of the states permit collective bargaining over public employees wages and benefits¹.

- 23 states and the District of Columbia extend full collective bargaining rights to all public employees².
- 13 states protect bargaining rights for some public employees².
- 14 states do not offer such coverage for any of their state and local government employees².

¹ *Governing Magazine* and Syracuse University's Maxwell School February 1999 report

² Public Employee Department, AFL-CIO

Retiree Medical

Pre 65 Retiree Medical Coverage

- All 50 state government employers offer health care benefits for retirees under the age of 65.

Age 65 and Older Retiree Medical Coverage

- 48 states (all but Indiana and Nebraska) offer health care benefits to retirees age 65 and older.

Source: Workplace Economics, July 2004

HRA / HSA Comparison (Page 1 of 5)

▪Issue	▪Health Reimbursement Arrangements	▪Health Savings Accounts
▪Eligibility	<ul style="list-style-type: none"> ▪ HRAs may be offered to current and former employees and individuals electing COBRA. ▪ No restriction for individuals covered by Medicare 	<ul style="list-style-type: none"> ▪ Employees, retirees, and the self-employed who are covered under a high-deductible health plan, but not covered under any other health plan (vision, dental plans exceptions) ▪ Medicare-eligible individuals cannot make contributions, but can draw down HSA balances.
▪Ownership	▪Employer Ownership	▪Employee Ownership
▪Employee Contributions	▪No. Employee contributions prohibited.	▪Yes, optional. Pre-tax (under a cafeteria plan) or post-tax contributions permitted.
▪Employer Contributions	▪Yes, required	▪Yes, optional
▪Tax Treatment of Employee Contributions	▪Not applicable.	<ul style="list-style-type: none"> ▪ Pre-tax contributions are excludable from employee's taxable gross income. ▪ Post-tax contributions can be taken as an "above the line" deduction.
▪Tax Treatment of Employer Contributions	▪Employer contributions are excludable from employee's taxable gross income.	▪Employer contributions whether direct or via pre-tax salary reductions (considered employer contributions for tax purposes) are excludable from employee's taxable gross income.
▪Maximum Deduction and Exclusion Rule on Contributions	▪No statutory limit, but benefits for highly compensated employees may be limited by the application of non-discrimination rules under code 105(h)	▪The deduction and exclusion for contributions to an HSA cannot exceed the lesser of the applicable deductible under the HDHP or the statutory maximum.
▪Employee Tax Impact	▪Claim reimbursements are tax free	▪Contributions are tax free, claims reimbursements are tax free
▪Employer Tax Savings	▪Business expense deduction for payments	▪Business expense deduction for employer contributions, plus employer FICA savings (7.65%) on employee contribution

HRA / HSA Comparison (Page 2 of 5)

▪Issue	▪Health Reimbursement Arrangements	▪Health Savings Accounts
▪Tax Treatment of Earnings	▪N/A	▪Earnings on HSA assets are not subject to tax while they are held in the HSA and are never taxed if they are distributed to reimburse for qualified medical expenses.
▪Portability	▪Yes, but at the Employer's discretion	▪Yes, completely (Legislated)
▪Funding Basis	▪Notional or Actual at employer's discretion	▪Actual Funding
▪Funding Requirements	<ul style="list-style-type: none"> ▪ Commonly designed as "virtual accounts" with reimbursements made from employer's general assets as claims occur. ▪ The account may be, but is not required to be, pre-funded by the employer 	▪Must be funded in a trust or custodial account.
▪High Deductible Health Plan (HDHPs)	<ul style="list-style-type: none"> ▪ Flexible; can be defined by employer as any design it likes, and there is no lower limit to deductible. ▪ Not required to be offered in conjunction with an HDHP. 	<ul style="list-style-type: none"> ▪ Compatible with a HDHP and legislated for 2005: ▪ HDHP must have an annual deductible of at least \$1,000 for single coverage, \$2,000 for family coverage. ▪ Out-of-pocket expense requirement can not exceed \$5,000 for single coverage, \$10,000 for family coverage.
▪Number of Accounts	▪Presumably, an employer could design an HRA with sub-accounts for particular family members, but there appears no tax advantage in doing so.	▪An HSA may be established for each spouse covered under an HDHP but they are subject to the combined deduction limit. Spouses may not jointly own a single HSA.
▪First Dollar Coverage Carve-outs	▪Employer's discretion	▪Allowed only for wellness benefits, prescription drugs for the treatment of specified chronic conditions, dental, vision
▪Coverage Tiers	▪Employer's discretion	▪Employee Only and Employee + Family are only two allowed coverage tiers

HRA / HSA Comparison (Page 3 of 5)

▪Issue	▪Health Reimbursement Arrangements	▪Health Savings Accounts
▪ Reimbursable Expenses	▪May reimburse for medical expenses defined in Section 213(d), including amounts paid for health plan premiums and long-term care coverage premiums, but cannot reimburse expenses for long-term care services.	<ul style="list-style-type: none"> ▪ May reimburse for medical expenses defined in Sec. 213(d) of the Internal Revenue Code. ▪ Generally cannot be used to pay for health plan premiums (exceptions include COBRA, long-term care premiums, premiums for non-Medigap premiums for people over age 65).
▪ Claim Substantiation Requirements	▪Medical care expenses must be substantiated.	<ul style="list-style-type: none"> ▪ Yes, upon audit ▪ Employers and HSA trustees are not required to determine whether HSA distributions are used exclusively for qualified medical expenses. HSA holders should maintain supporting records. ▪ Substantiation likely required under HDHP.
▪ Claims Processing	▪Usually automatic, sometimes debit card	▪Debit Card or Automatic
▪ Employer Reporting Requirements	▪Not required.	▪Employer contributions must be reported on the employee's Form W-2.
▪ Surviving Spouse	▪May depend on the terms of the particular HRA and application of COBRA.	▪The surviving spouse who is the beneficiary of the HSA becomes the new account beneficiary.
▪ Estate or Other Beneficiary	▪May depend on the terms of the particular HRA and application of COBRA.	▪On the date of death, the HSA loses its status as an HSA; in general, the estate or other non-spouse beneficiary will be subject to an income tax in an amount equal to the fair market value of the assets.
▪ COBRA	▪COBRA is applicable, but it is unclear how the account dollars are shared among potential beneficiaries.	▪COBRA is inapplicable to HSAs, but it would apply to an HDHP that is an employer plan.

HRA / HSA Comparison (Page 4 of 5)

Issue	Health Reimbursement Arrangements	Health Savings Accounts
▪HIPAA Applies?	▪Yes	▪Yes, if claims adjudicated
Investment Options	Generally none, as accounts are unfunded.	Depends upon provider of HSA, but active investment of assets is a common feature
Financial Partner Required?	No	Yes
Financial Incentives	Offered to employees (e.g., if employees complete a health assessment test)	Not offered in conjunction with HSA balances
Account retained by employee upon termination	Generally no; however, at employer's discretion as to whether terminated employees may be covered	Yes
Cash-Out Options?	None generally, although this is at the employer's discretion (though would be a taxable event to the employee)	No penalty if over the age of 65, but 10% penalty if pre-65
Ability to roll-over funds?	Yes, employer's discretion	Yes
Funds revert to employer upon termination?	Yes, employer's discretion	No
Ability to convert account to taxable income	No	Yes
Insurance premiums paid from account	Yes	Yes
Long Term Care premiums	Yes	Yes
Banking	Employer Assets	IRA type account

HRA / HSA Comparison (Page 5 of 5)

▪Issue	▪Health Reimbursement Arrangements	▪Health Savings Accounts
<p>▪Issues Related to Converting from HRA to HSA</p>	<ul style="list-style-type: none"> ▪ HRA costs are realized when medical claims are presented and paid against the account. Rollover balances and forfeitures do not represent cash outlays. Conversion to HSAs will require the employer to incur a cash expense for all HRA balances to be rolled into the HSA. ▪ Generally speaking, the HRA's flexibility and the fact that it is a notional account make it a better choice for employer funded accounts. ▪ Note that at present, there is no provision under the law for HRA rollovers to HSA accounts that exceed current year funding limits on HSAs. There are proposed bills to allow such a rollover, but the size of existing HRA account balances may be a complicating factor at present. 	<ul style="list-style-type: none"> ▪ HSA costs are realized as the employer deposits funds into an employee's account. ▪ All things being equal, employees will generally view HSAs more favorably because they are funded and portable. However, all things are seldom equal. The HSA will not be viewed favorably if the employee is the sole source of account funding. ▪ Employers must realize that on an ongoing basis, HSAs will have a higher net cost than HRAs (assuming the same level of employer contributions to HSA as to HRA)